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No. 79-1423

In the Supreme Court of the United States

OCTOBER TERM, 1980

THE WESTERN AND SOUTHERN LIFE INSURANCE COMPANY, APPELLANT

v.

STATE BOARD OF EQUALIZATION OF THE STATE OF CALIFORNIA

ON APPEAL FROM THE COURT OF APPEAL SECOND APPELLATE DISTRICT, STATE OF CALIFORNIA

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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This brief is submitted in response to the Court's invitation of May 12, 1980.

QUESTIONS PRESENTED

1. Whether Section 685 of the California Insurance Code violates the Equal Protection Clause of the Fourteenth Amendment by subjecting appellant, an Ohio

insurance company, to higher taxes than California insurance companies because Ohio, without distinction between foreign and domestic insurance companies, imposes greater taxes upon insurance companies than California imposes on domestic insurance companies.

2. Whether Section 12241 of the Cal. Rev. & Tax. Code violated appellant's Fourteenth Amendment right to equal protection of the laws by denying a substantial part of the credit against its premium taxes in the amount of the real estate taxes on its principal office in California that would otherwise be allowable to an in-state insurance company.

3. Whether the California tax statutes imposing heavier tax burdens on out-of-state insurance companies unconstitutionally discriminate against interstate commerce.

4. Whether the McCarran-Ferguson Act, 15 U.S.C. 1011–1015, authorizes California's statutory discrimination against interstate commerce.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Constitutional provisions and statutes involved	1
Statement	3
Argument	8
Conclusion	16

TABLE OF AUTHORITIES

Cases:

A&P Tea Co. v. *Cottrell*, 424 U.S. 366	9
Atlantic Ins. Co. v. *State Board of Equalization*, 255 Cal. App.2d 1, 62 Cal. Rptr. 784	5, 7
Boston Stock Exchange v. *State Tax Comm'n*, 429 U.S. 318	10, 11
FTC v. *National Casualty Co.*, 357 U.S. 560	12
FTC v. *Travelers Health Ass'n*, 362 U.S. 293	12
Franklin Life Ins. Co. v. *State Board of Equalization*, 63 Cal.2d 222, 404 P.2d 477, 45 Cal. Rptr. 869	5
Group Life & Health Ins. Co. v. *Royal Drug Co.*, 440 U.S. 205	12, 15
Hanover Fire Ins. Co. v. *Harding*, 272 U.S. 494	10
Hood & Sons v. *DuMond*, 336 U.S. 525	12
Ky. Whip & Collar Co. v. *I.C.R. Co.*, 299 U.S. 334	12

Cases—Continued: Page

Lewis v. *BT Investment Managers, Inc.*, No. 79-45 (June 9, 1980) 11, 12
Maryland Casualty Co. v. *Cushing*, 347 U.S. 409 12
Northwestern States Portland Cement Co. v. *Minnesota*, 358 U.S. 450 10
Philadelphia v. *New Jersey*, 437 U.S. 617 .. 11
Prudential Insurance Co. v. *Benjamin*, 328 U.S. 408 ..... 12, 15, 16
Prudential Insurance Co. v. *Hobbs*, 328 U.S. 822 16
Prudential Insurance Co. v. *Indiana*, 328 U.S. 823 16
Reserve Life Ins. Co. v. *Bowers*, 380 U.S. 258 10
Robertson v. *California*, 328 U.S. 440 13
St. Paul Fire & Marine Ins. Co. v. *Barry*, 438 U.S. 531 ..... 12, 15
SEC v. *National Securities, Inc.*, 393 U.S. 453 12
SEC v. *Variable Annuity Life Insurance Co.*, 359 U.S. 65 12
Scott v. *Donald*, 165 U.S. 58 12
Southern Ry. v. *Greene*, 216 U.S. 400 10
State Bd. of Ins. v. *Todd Shipyards*, 370 U.S. 451 ..... 8, 12
Toomer v. *Witsell*, 334 U.S. 385 9
United States v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 12
Western & Southern Life Ins. Co. v. *State Board of Equalization*, 4 Cal. App.3d 21, 84 Cal. Rptr. 88 ..... 5, 6

Cases—continued: Page

Wheeling Steel Corp. v. *Glander*, 337 U.S. 562 10
Whitfield v. *Ohio*, 297 U.S. 431 12
WHYY v. *Glassboro*, 393 U.S. 117 ..... 8, 10

Constitutions and statutes:

United States Constitution:
Article I, Section 8, Clause 3 1
Fourteenth Amendment, Section 1 ..... 2, 7, 8, 10
California Constitution, Article XIII:
Section 14–4/5(e) 6
Section 14–4/5(f)(3) 4
McCarran-Ferguson Act, 15 U.S.C. 1011–1015 8
15 U.S.C. 1011–1013 2
15 U.S.C. 1012 14
15 U.S.C. 1013 14
Cal. Ins. Code (West 1972):
Section 685 ..... 4, 5, 8, 9, 10
Section 701 3
Cal. Rev. & Tax. Code (West 1970):
Section 12201 4
Section 12202 4
Section 12204 4
Section 12221 4
Section 12241(a) 6
Section 12241(b) 6, 8, 10

Miscellaneous:

91 Cong. Rec. (1945):
pp. 478–488 14
p. 482 14–15

Miscellaneous—Continued: Page

p. 1085 14
p. 1085–1094 14
p. 1092 14
p. 1396 14
p. 1442 14
pp. 1442–1444 14
pp. 1477–1489 14
H.R. Rep. No. 143, 79th Cong., 1st Sess. (1945) 13
S. Rep. No. 20, 79th Cong., 1st Sess. (1945) 14

OPINIONS BELOW

The order of the trial court and its Memorandum of Intended Decision and Conclusions of Law (J.S. App. 1a–24a) are not officially reported. The opinion of the Court of Appeal (J.S. App. 27a–34a) prior to its modification (J.S. App. 35a–36a) is reported at 99 Cal. App. 3d 410, 159 Cal. Rptr. 539. The order of the Supreme Court of California denying hearing (J.S. App. 36a) is unreported.

JURISDICTION

The judgment of the Court of Appeal in favor of the validity of provisions of the Constitution and statutes of the State of California, the validity of which were drawn in question on the ground of repugnance to the Constitution of the United States, was entered on November 2, 1979 (J.S. App. 27a). The Court of Appeal denied a petition for rehearing on November 28, 1979 (J.S. App. 35a–36a). The Supreme Court of California denied a petition for hearing on December 27, 1979 (J.S. App. 36a). The notice of appeal to this Court was filed on February 11, 1980 (J.S. App. 37a–38a), and the Jurisdictional Statement was filed on March 13, 1980. The jurisdiction of this Court is invoked under 28 U.S.C. 1257(2).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Article I, Section 8, Clause 3 of the United States Constitution (the Commerce Clause) provides: "The Congress shall have Power * * * To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

Section 1 of the Fourteenth Amendment to the United States Constitution provides: "* * *No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State * * * deny to any person within its jurisdiction the equal protection of the laws."

The relevant provisions of the McCarran-Ferguson Act, 15 U.S.C. 1011–1013, are as follows:

> § 1011. *Declaration of Policy.*—Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.
>
> § 1012. *Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948.*—(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1980, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended [15 U.S.C. 41 *et seq.*], shall be applicable to the business of insurance to the ex-

tent that such business is not regulated by State Law.

§ 1013. *Suspension until June 30, 1948, of application of certain Federal laws; Sherman Act applicable to agreements to, or acts of, boycott, coercion, or intimidation.*—(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act [15 U.S.C. 41 *et seq.*], and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

The relevant provisions of the Constitution and Statutes of the State of California are set forth in J.S. App. 41a–46a.

STATEMENT

1. Appellant brought this action in the Superior Court of the State of California for the County of Los Angeles to recover California taxes that it paid under protest for the period 1965–1971.

The facts were stipulated (J.S. App. 3a–4a) and may be summarized as follows: Appellant is an Ohio mutual life and disability insurance company which has its principal office in that State. Pursuant to Section 701 of the Cal. Ins. Code (West 1972),[1] appellant qualified

[1] Section 701 of the Cal. Ins. Code (West 1972) provides that a certificate of authority "shall be for an indefinite term and shall

to do business in California and was issued a Certificate of Authority for an indefinite term on July 1, 1956. Appellant has conducted a life and disability insurance business in California continuously since the issuance of its Certificate of Authority. Prior to 1965, appellant constructed an office building on land it owned in Los Angeles, and established its principal California office in that building. It has continued to maintain its principal California office in that building. However, appellant leases approximately 76% of the space in the building to tenants not related to its operations (J.S. App. 4a, 29a).

a. Pursuant to Sections 12201, 12202, and 12221 of the Cal. Rev. & Tax. Code (West 1970), California imposes upon every insurer doing business in the State, with exceptions not here relevant, an annual tax at a rate slightly in excess of 2.3% of gross premiums, less return premiums, received by the insurer upon business done in the State. Section 12204 of the Cal. Rev. & Tax. Code (West 1970) generally provides that this gross premium tax is, with stated exceptions, "in lieu of all other taxes, State, county, and municipal, upon such insurers and their property." Among the stated exceptions are taxes upon insurance companies' real estate and the so-called retaliatory tax authorized by Article XIII, Section 14–4/5(f)(3) of the California Constitution and imposed by Section 685 of the Cal. Ins. Code (West 1972) (J.S. App. 41a–43a). This latter provision addresses the case of an insurer doing business in California but incorporated in another state,

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expire with the expiration or termination of a corporate existence of the holder thereof."

where the state of incorporation would (even though without differentiation between domestic and out-of-state insurers) impose upon California insurers doing business in that state a greater amount of taxes than California would impose upon insurers of the other state doing business in California. In these circumstances, the California retaliatory tax requires that insurers of the other state (in addition to the tax otherwise imposed) pay an additional amount that would bring the total taxes and fees payable to California up to the amount that would have been payable to the other state.[2]

Acting under Section 685 of the Ins. Code, the State Board of Equalization issued a retaliatory tax assessment of $128,214.90 for 1965, and lesser amounts for the succeeding years through 1971, all of which appellant paid under protest.[3] It was stipulated that Ohio

[2]Prior to 1965, this retaliatory tax was imposed upon out-of-state insurers doing business in California only if their state discriminated against California insurers doing business in that other state, and in favor of domestic insurers. In 1964, however, the California Constitution was amended, and, since 1965, California has imposed the retaliatory tax upon out-of-state insurers doing business in California simply because the level of taxation upon insurers in their home state, undifferentiated between domestic and out-of-state insurers, is higher than the level of taxation upon insurers in California. See *Western & Southern Life Ins. Co.* v. *State Board of Equalization*, 4 Cal. App.3d 21, 84 Cal. Rptr. 88 (1970); *Atlantic Ins. Co.* v. *State Board of Equalization*, 255 Cal. App.2d 1, 62 Cal. Rptr. 784 (1967); *Franklin Life Ins. Co.* v. *State Board of Equalization*, 63 Cal.2d 222, 404 P.2d 477, 45 Cal. Rptr. 869 (1965).

[3]The retaliatory tax is computed as an amount in excess of the premiums tax. The amount of the premiums tax is also in contest for 1966–1971 (see *infra*, pages 6–7). Hence, the amounts of the two taxes for the years after 1965 are not separately designated. The aggregate amount in issue is $977,853.57, plus interest (J.S. App. 24a, 26a).

does not impose upon California insurers doing business in Ohio greater taxes, fees, etc. than upon domestic insurers doing business in Ohio, and the trial court so found (J.S. 6 n.2; J.S. App. 10a, 21a).[4]

b. Section 12241(a) of the Cal. Rev. & Tax. Code (West 1970) allows an insurer a credit against the annual premiums tax equal to the real estate taxes paid for the same year on real property owned by it on which was located its home office or principal office in the state.[5] In accordance, however, with an amendment to Article XIII, Section 14–4/5(e) of the California Constitution adopted in 1966, Section 12241(b) has provided thereafter that where a portion of the real property constituting the home or principal office was occupied by any person or persons other than the insurer, the credit allowed by Section 12241(a) is proportionately reduced. This reduction in the credit, however, is not applicable to insurers organized under the laws of California before December 31, 1966. As a result of these statutory provisions, appellant's credit against its premium taxes was reduced by approximately 76%, while similarly-situated California insurers suffered no reduction at all in their credit.

2. Appellant paid both the retaliatory tax assessments and the additional premiums taxes for 1966–1971 under protest, the latter because of the reduced "principal office" credit (J.S. App. 3a–4a). It thereafter filed claims for refund of the retaliatory taxes and

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[4]See also *Western & Southern Life Ins. Co.* v. *State Board of Equalization*, 4 Cal. App.3d 21, 84 Cal. Rptr. 88 (1970).

[5]This credit was repealed in 1976, effective January 1, 1977 (J.S. App. 16a).

the amount of the premiums taxes paid under protest, and, when those claims were denied, brought this action for refund of the taxes in issue in the Superior Court.

The Superior Court entered judgment in favor of appellant for the full amount of the refunds sought, plus statutory interest (J.S. App. 24a, 26a). It held that in discriminating against corporations engaged in interstate commerce and in favor of domestic corporations, both the retaliatory tax and the limits on the "principal office" credit violated the Commerce Clause and appellant's rights to due process and equal protection as guaranteed by the Fourteenth Amendment. The court also held that the California retaliatory tax was not authorized by the McCarran-Ferguson Act (J.S. App. 3a–24a).

The Court of Appeal reversed. It held that the retaliatory tax was authorized by the McCarran-Ferguson Act (J.S. App. 30a–31a). On the authority of its earlier decision in *Atlantic Ins. Co.* v. *State Board of Equalization*, 255 Cal. App. 2d 1, 62 Cal. Rptr. 784 (1967), the court held that the retaliatory tax did not violate either the commerce clause or appellant's right to equal protection of the laws under the Fourteenth Amendment (J.S. App. 32a–33a). The court stated with respect to *Atlantic Ins. Co.*, "Right or wrong, we feel impelled to follow it in the case before us" (J.S. App. 33a). Finally, the Court of Appeal ruled that it did not have to address the limits of the "principal office" credit allowed out-of-state insurers because to the extent that appellant's premiums tax was reduced, its retaliatory tax would be increased (J.S. App. 33a–

34a). The Court of Appeal denied a petition for rehearing (J.S. App. 35a–36a), and the Supreme Court of California denied appellant's petition for hearing (J.S. App. 36a).

ARGUMENT

The California tax statutes at issue in this case violate the Equal Protection Clause of the Fourteenth Amendment, and are inconsistent with the limitations imposed upon the States by the Commerce Clause. Moreover, the McCarran-Ferguson Act, 15 U.S.C. 1011–1015, does not relax the limitations that the Fourteenth Amendment imposes upon the States. *State Bd. of Ins.* v. *Todd Shipyards*, 370 U.S. 451 (1962). Nor should it be construed to authorize state action hostile to, and discriminatory against, out-of-state insurers engaged in interstate commerce in the manner of the California statutes.

1. Appellant qualified to do business in California in 1956. Since that time, it has held an indefinite license, coterminous under California law with its corporate existence, to do business as a life and disability insurer. Accordingly, the taxes here in question are not analogous to an entrance fee imposed by California upon a foreign corporation, as a condition of doing business within the state, of the type that the Court has upheld. See *WHYY* v. *Glassboro*, 393 U.S. 117, 119 (1968). On the contrary, the so-called retaliatory tax imposed by Section 685 of the Insurance Code, and the limitation on the "principal office" credit against the premiums tax imposed by Section 12241(b) of the

Revenue and Taxation Code, are burdens imposed upon appellant because it is a foreign corporation. Indeed, appellant is subject to the retaliatory tax solely because Ohio, its state of incorporation, imposes upon insurers, though in completely evenhanded fashion, a somewhat higher level of taxation than California.

We submit that California has no legitimate interest in Ohio's level of taxation or fiscal structure when no discriminatory action against California citizens or corporations is involved. Cf. *Toomer* v. *Witsell*, 334 U.S. 385, 395–407 (1948). The several states have different resources, populations, social and economic conditions, levels of public services, fiscal structures, methods and sources of raising revenue, and tax burdens, both in gross and per capita. With respect to other states, where no discriminatory or hostile action is involved, the states are largely autonomous in these matters. And even if another state has engaged in discriminatory action, as this Court has pointed out, the Constitution does not contemplate the economic warfare of reprisal and retaliation. *A&P Tea Co.* v. *Cottrell*, 424 U.S. 366 (1976).

Since Ohio does not in fact discriminate against California or other insurers, there is no greater justification for the tax imposed by Section 685 of the Ins. Code than if California imposed upon Ohio residents who happened to own land in California a higher property tax than was otherwise imposed simply because the level of real property taxation in Ohio was higher than in California. Section 685 and the limitation upon the "principal office" credit mandated by Section

12241(b) of the Rev. & Tax. Code[6] constitute tax burdens imposed upon foreign insurance corporations because they are foreign corporations. The decisions of this Court have uniformly struck down such discriminatory taxation as violative of the Equal Protection Clause of the Fourteenth Amendment. *E.g.*, *WHYY* v. *Glassboro*, 393 U.S. 117 (1968); *Reserve Life Ins. Co.* v. *Bowers*, 380 U.S. 258 (1965); *Wheeling Steel Corp.* v. *Glander*, 337 U.S. 562 (1949); *Hanover Fire Ins. Co.* v. *Harding*, 272 U.S. 494 (1926); *Southern Ry.* v. *Greene*, 216 U.S. 400 (1910).

2. Throughout the history of this Court's decisions involving state taxation of interstate commerce, there have been "some firm peaks of decision which remain unquestioned." *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450, 457 (1959). "Among these is the fundamental principle that * * *: No State, consistent with the Commerce Clause, may 'impose a tax which discriminates against interstate commerce * * * by providing a direct commercial advantage to local business.'" *Boston Stock Exchange* v. *State Tax Comm'n*, 429 U.S. 318, 329 (1977). There, the Court held that New York could not impose a tax "to favor local commercial interests over out-of-state businesses," even though the discrimination was "between two types of interstate transactions" (429 U.S. at 335).

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[6] If, as we believe, Section 685 of the Insurance Code is unconstitutional, it is no longer possible to avoid, as did the Court of Appeal, passing upon the constitutionality of the discriminatory aspects of the "principal office" credit limitation imposed by Section 12241(b) of the Rev. & Tax. Code (see J.S. App. 33a–34a).

Only last Term, the Court applied the same criteria in striking down, under the Commerce Clause, a Florida statute that prohibited an out-of-state bank holding company from owning or controlling a business furnishing investment advisory services to the general public. *Lewis* v. *BT Investment Managers, Inc.*, No. 79–45 (June 9, 1980). As the Court there observed, "where simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected," quoting from *Philadelphia* v. *New Jersey*, 437 U.S. 617, 624 (1978).

Judged by these standards, the California statutes here in question would appear, if standing alone, to be inconsistent with the Commerce Clause, and the court below did not assert otherwise. The remaining question is whether the McCarran-Ferguson Act should be construed to permit the "simple economic protectionism" exemplified by the California statutes involved in the case.

We think not and submit that the history and purpose of the McCarran-Ferguson Act demonstrate that it should not. But we start with a more fundamental premise. As the Court pointed out in *Boston Stock Exchange*, quoting from earlier decisions, "[t]he very purpose of the Commerce Clause was to create an area of free trade among the several States" (429 U.S. at 328). An Act of Congress should therefore not be construed to frustrate that purpose unless by its explicit terms the legislation authorizes the practice of economic protectionism by the States. Indeed, on several occasions, this Court has declined to construe federal statutes to permit state action that would have

excluded or discriminated against out-of-state competition, even where the federal statute authorized State regulation. *Lewis* v. *BT Investment Managers, Inc.*, No. 79–45 (June 9, 1980), slip op. 16–21; *Hood & Sons* v. *DuMond*, 336 U.S. 525, 540–545 (1949); *Scott* v. *Donald*, 165 U.S. 58, 100 (1897). And where the Court upheld earlier federal legislation with respect to interstate shipments that reinforced or authorized state restrictions on the sale of interstate goods, the Court was careful to point out that the restrictions were nondiscriminatory. *Ky. Whip & Collar Co.* v. *I.C.R. Co.*, 299 U.S. 334, 351 (1937); *Whitfield* v. *Ohio*, 297 U.S. 431, 439–440 (1936).

The McCarran-Ferguson Act was passed in response to this Court's decision in *United States* v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944).[7] In that case, the Court held that multi-state insurers were engaged in commerce among the several States, and were subject to the provisions of the Sherman Antitrust Act, 15 U.S.C. 1 and 2. Many people professed to believe that the decision effectively immunized multi-state insurers, and a large part of the business of insurance, from state regulation and from state taxa-

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[7] This Court has examined the legislative history of the McCarran-Ferguson Act in a substantial number of cases. See, *e.g.*, *Group Life & Health Ins. Co.* v. *Royal Drug Co.*, 440 U.S. 205 (1979); *St. Paul Fire & Marine Ins. Co.* v. *Barry*, 438 U.S. 531 (1978); *SEC* v. *National Securities, Inc.*, 393 U.S. 453 (1969); *State Bd. of Ins.* v. *Todd Shipyards*, 370 U.S. 451 (1962); *FTC* v. *Travelers Health Ass'n*, 362 U.S. 293 (1960); *SEC* v. *Variable Annuity Life Insurance Co.*, 359 U.S. 65 (1959); *FTC* v. *National Casualty Co.*, 357 U.S. 560 (1958); *Maryland Casualty Co.* v. *Cushing*, 347 U.S. 409 (1954); *Prudential Insurance Co.* v. *Benjamin*, 328 U.S. 408 (1946).

tion. That such a belief was greatly overdrawn was demonstrated not only by the Court's subsequent decision in *Robertson* v. *California*, 328 U.S. 440 (1946), but also by the contemporaneous treatment of interstate carriers and of manufacturers, wholesalers, and others engaged in interstate commerce on a large scale. Congress, nevertheless, felt impelled to act. The reason for action and the intended scope of action are well described in the Report of the House Committee on the Judiciary, H.R. Rep. No. 143, 79th Cong., 1st Sess. 2–3 (1945), as follows:

> Inevitable uncertainties which followed the handing down of the decision in the *Southeastern Underwriters Association case*, with respect to the constitutionality of State laws, have raised questions in the minds of insurance executives, State insurance officials, and others as to the validity of State tax laws as well as State regulatory provisions; thus making desirable legislation by the Congress to stabilize the general situation.
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> * * * Your committee believes there is urgent need for an immediate expression of policy by the Congress with respect to the continued regulation of the business of insurance by the respective States. Already many insurance companies have refused, while others have threatened refusal to comply with State tax laws, as well as with other State regulations, on the ground that to do so, when such laws may subsequently be held unconstitutional in keeping with the precedent-smashing decision in the *Southeastern Underwriters case*, will subject insurance executives to both civil and criminal actions for misappropriation of company funds.
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> * * * * *

> It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association case.*

The pertinent Senate report, S. Rep. No. 20, 79th Cong., 1st Sess. (1945), is largely to the same effect. In presenting the Conference Report to the Senate, Senator McCarran read from the Report of the House Judiciary Committee, and added, "In other words, we give to the States no more powers than those they previously had, and we take none from them." 91 Cong. Rec. 1442 (1945).

The congressional debate principally concerned antitrust legislation—whether it should be suspended, partially suspended, restored after a period of suspension, etc. See 91 Cong. Rec. 478–488, 1085–1094, 1396, 1442–1444, 1477–1489 (1945).[8] The uncertainties of state taxation of insurance companies are mentioned from time to time, but rarely more than briefly.[9] Typical was Representative Springer's remark that the pending measure would allow the states "to collect the taxes now permitted—all without Government interference." 91 Cong. Rec. 1092 (1945). See also, *e.g.*, 91

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[8] Sections 2 and 3 of the Act, 15 U.S.C. 1012 and 1013, embody the compromises that were reached after extended discussions.

[9] For example, Representative Walter reported to the House that the Attorney General of North Carolina had ruled that the State could no longer collect taxes paid by insurance companies. See 91 Cong. Rec. 1085 (1945).

Cong. Rec. 482 (1945) (Senator Radcliffe, "The right of the States * * * to collect taxes should not be terminated"). There is nothing explicit in the debate, the committee reports, or the statute that suggests that the states were given authority to erect barriers of economic protectionism. Insofar as state taxes were concerned, Congress was aware that current state revenues were in jeopardy of interruption, and intended to remove that hazard and uncertainty. Nothing suggests that Congress ever considered, or that the states were in fact given, enhanced authority to exclude, or to interfere with, competition by out-of-state insurers. And this Court's decisions under the McCarran-Ferguson Act have not in other respects construed the Act to sanction anticompetitive arrangements.[10] There is no reason why the tax provisions should be construed to permit anticompetitive taxation that discriminates against out-of-state insurers.

Prudential Insurance Co. v. *Benjamin*, 328 U.S. 408 (1946), principally relied upon by the court below (J.S. App. 12a–14a), is not to the contrary. The principal thrust of that decision was to establish the power of Congress, challenged by the appellant in that case, to authorize the states to take action that, in the absence of congressional action, might be deemed to be inconsistent with the Commerce Clause. What Congress had in fact authorized received lesser consideration. In that the Court was explicit: "It is not neces-

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[10] See, *e.g.*, *Group Life & Health Ins. Co.* v. *Royal Drug Co.*, 440 U.S. 205 (1979); *St. Paul Fire & Marine Ins. Co.* v. *Barry*, 438 U.S. 531 (1978).

sary to spend much time with interpreting the McCarran Act" (328 U.S. at 429). The Court refrained from addressing the question whether the South Carolina tax in issue was in fact discriminatory (*id.* at 428), and did not rule upon the validity of any state statute not substantially identical with that of South Carolina (*id.* at 437 n.40). There is no reason to believe that *Prudential Insurance Co.* v. *Hobbs*, 328 U.S. 822 (1946) and *Prudential Insurance Co.* v. *Indiana*, 328 U.S. 823 (1946), both decided per curiam a week later on the authority of *Benjamin*, decided more than the principal decision. In sum, unlike *Prudential*, the question in this case does not involve the scope of Congress's power. It simply involves the proper construction of legislation that Congress enacted. We believe that it should not be construed to uphold California's statutory protectionism.

CONCLUSION

Probable jurisdiction should be noted.

Respectfully submitted.

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